

IN THE UNITED STATES DISTRICT COURT  
FOR THE EASTERN DISTRICT OF CALIFORNIA

UNITED STATES OF AMERICA, CASE NO. CV F 05-0594 LJO SMS

Plaintiff,

**ORDER ON GOVERNMENT'S PERMANENT  
INJUNCTION AND SANCTIONS MOTIONS**  
(Docs. 122, 129.)

vs.  
STEVE HEMPFLING, d/b/a  
FREE ENTERPRISE SOCIETY,

Defendant.

**INTRODUCTION**

Plaintiff United States of America (“Government”) seeks to enjoin permanently defendant Steve Hempfling (“Mr. Hempfling”), d/b/a Free Enterprise Society, to promote, organize and sell abusive tax evasion and shelter products and to provide information on purchasers of such products.<sup>1</sup> The Government further seeks a default judgment against Mr. Hempfling as a discovery sanction for Mr. Hempfling’s disobedience of orders and failure to participate in discovery, including not appearing at his deposition. Mr. Hempfling fails to address the substantive merits of the Government’s claims and

<sup>1</sup> Although the Government styles its papers as a summary judgment motion, this Court construes the Government’s papers as a dispositive motion for a permanent injunction. This Court carefully reviewed and considered all arguments, points and authorities, declarations, depositions, exhibits, objections and other papers filed by the parties. Omission of reference to an argument, document, paper or objection is not to be construed to the effect that this Court did not consider the argument, document, paper or objection. This Court thoroughly reviewed and considered the evidence it deemed admissible, material and appropriate for its ruling.

1 effectively fails to challenge meaningfully the Government’s requested relief in an apparent attempt to  
2 continue to obstruct a rightful decision on the merits of the Government’s claims. This Court  
3 considered the Government’s permanent injunction and sanctions motions on the record and VACATES  
4 the March 17, 2007 hearing, pursuant to Local Rule 78-230(h). As discussed in greater detail below,  
5 this Court IMPOSES a terminating discovery sanction and ENJOINS Mr. Hempfling to promote,  
6 organize and sell abusive tax shelters, plans or arrangements to incite attempts to violate internal revenue  
7 laws, to evade unlawfully assessment or collection of federal tax liabilities, or to claim improper tax  
8 refunds.

## BACKGROUND

## Mr. Hempfling And The Free Enterprise Society

11 Mr. Hempfling is identified as the Director and an original founder of the Free Enterprise Society  
12 in its promotional literature and on its website. The Free Enterprise Society is located in Fresno.  
13 According to its Information Package & Freedom Catalog #10 ("Catalog #10"), the Free Enterprise  
14 Society was founded by Mr. Hempfling and two other men and that its purpose "is to restore the  
15 government to its constitutionally restricted activities and rid society of income tax." The Free  
16 Enterprise Society has sponsored rallies at which Mr. Hempfling has been a speaker. Through its  
17 Catalog #10 and website, the Free Enterprise Society sells products, including the "Reliance 2000  
18 Program," "W4 Alternative Withholding Package," and "IRS Lien and Levy Package."

## **The Reliance 2000 Program**

According to Catalog #10, the Reliance 2000 Program is designed by the Free Enterprise Society and William J. Benson (“Mr. Benson”), coauthor of *The Law That Never Was*. The Reliance 2000 Program comprises two volumes of *The Law That Never Was* and the “16<sup>th</sup> Amendment Reliance Package.” Catalog #10 sets out four steps for the Reliance 2000 Program:

- 1       3.     **“Redress of Grievance Letter Package.** This contains the letters for you to send to the
- 2              President, Congressman, your Senators and others for the ‘redress of grievance’ you have
- 3              over the 16<sup>th</sup> Amendment issue. . . .”
- 4       4.     **“File a federal lawsuit** asking for an answer to the 16<sup>th</sup> Amendment question. **You**
- 5              **want to follow the law if only you knew what the law was.** For more information on
- 6              the above 4 steps, you should order seminars 9201 and/or 9202. Lawsuit price starts at
- 7              150.00 and is available only to current members of the Society & Civil Support Service.”
- 8              (Bold in original and added.)

9              The cover of the 16<sup>th</sup> Amendment Reliance Package, acquired by the Internal Revenue Service  
10 (“IRS”), states that it had been developed by the Free Enterprise Society and Constitutional Research  
11 Associates. The 16<sup>th</sup> Amendment Reliance Package’s inside cover notes that it was copyrighted in 1992  
12 by Mr. Benson of Constitutional Research Associates and published by the Free Enterprise Society.

13              The Government notes that Mr. Hempfling knows or has reason to know that his statements in  
14 the 16<sup>th</sup> Amendment Reliance Package about the 16<sup>th</sup> Amendment’s validity and internal revenue laws  
15 are false or fraudulent. The Government points out that the 16<sup>th</sup> Amendment Reliance Package includes  
16 the decision *United States v. Benson*, 941 F.2d 598 (7<sup>th</sup> Cir. 1991), which held that Mr. Benson was not  
17 entitled to an evidentiary hearing on 16<sup>th</sup> Amendment’s validity because the issue was “beyond review.”

18              The W4 Alternative Withholding Package

19              The W4 Alternative Withholding Package states: “Glaringly apparent is the fact that no statute  
20 exists which imposes a tax on the income of U.S. citizens living and domiciled in the United States.  
21 There is simply no statutory provision for this class of people to make returns or pay an income tax,  
22 unless of course, such person was acting as a withholding agent.” In its own words, the W4 Alternative  
23 Withholding Package “attempts to correct the error in, or establish the correctness of, your withholding  
24 status for income tax purposes at the administrative level.” The W4 Alternative Withholding Package  
25 continues: “Keep in mind that the W-4/DE-4 Form only applies to non-resident aliens, resident aliens,  
26 and U.S. Citizens working abroad.”

27              The W4 Alternative Withholding Package instructs purchasers to: (1) prepare a notarized  
28 declaration that he/she is “an inhabitant and Citizen of the Republic of the State of [YOUR STATE],

1 and by virtue of Article 4, Section 2, Clause 1 of the Constitution for the United States of America, is  
2 also a United States citizen claiming to be a person not subject to withholding”; and (2) send the  
3 notarized declaration to the purchaser’s employer to “correct” the purchaser’s withholding status. The  
4 Civil Support Service of the Free Enterprise Society offers to prepare for \$30 a custom “Withholding  
5 Declaration Package” and form letters to employers and the IRS and which the Government contends  
6 “falsely state that the purchaser is not subject to withholding.”

## **The IRS Lien And Levy Package**

The IRS Lien and Levy Package states: "In conclusion the Congress did not provide that the Internal Revenue Service could assess for a Form 1040, or other kind of Form, kind of tax, hence the lien and levy are legally unenforceable." The IRS Lien and Levy Package further states falsely, as characterized by the Government: "Treasury Regulation section 301.6323(f)-1 only provides form, but not content of the notice as required by Internal Revenue Code Sections 6323(a), and 6323(f)(3). Therefore the federal tax lien is legally unenforceable as a matter of law according to Internal Revenue Manual No. 5700, Special Procedures, Section 5717.23." The Government notes that based on false statements and interpretations of the Internal Revenue Code, IRS Lien and Levy Package purchasers are instructed to demand releases of IRS levies and liens and administrative claims for "illegally assessed taxes" and to use form letters provided in the IRS Lien and Levy Package.

## **Mr. Hempfling's Seminar Statements**

19 The Government notes that through his website and California and Nevada seminars, Mr.  
20 Hempfling “hawks his books, packages, tapes, and compact disks with promises of how they will assist  
21 customers to successfully become and remain non-filers.” The Government identifies Mr. Hempfling’s  
22 “tax-scheme” products as previously-recorded seminars, and the Reliance 2000 and Alternative W4  
23 Withholding packages. The Government notes that the products are marketed with promises of tax  
24 benefits, including reduction or elimination of withholdings. The Government points out that Greg Hill  
25 (“Mr. Hill”), the Legal Defense Director of the Free Enterprise Society, introduced Mr. Hempfling at  
26 a seminar by stating: “I’ve already done everything I’m asking you to do. What did I do? I quit filing.”

## The Government's Claims

<sup>28</sup> The Government proceeds on its operative first amended complaint under 26 U.S.C. §§ 7402(a).

1 and 7408 to enjoin Mr. Hempfling permanently to organize, promote and sell fraudulent tax schemes  
2 which promote that the Sixteenth Amendment was never ratified, that IRS liens and levies are  
3 unenforceable, and that no law requires filing of a W4 form.

4 **Mr. Hempfling's Initial Interlocutory Appeal**

5 This Court's February 22, 2006 order denied Mr. Hempfling's motion to dismiss the  
6 Government's first amended complaint. On March 1, 2006, Mr. Hempfling filed his notice for an  
7 interlocutory appeal of denial to dismiss the Government's first amended complaint. This Court's  
8 March 16, 2006 minute order noted that Mr. Hempfling had neither paid the required appeal fee nor  
9 obtained necessary certification of an interlocutory appeal. With its June 12, 2006 order, the Ninth  
10 Circuit Court of Appeals dismissed Mr. Hempfling's appeal.

11 This Court's May 1, 2007 order struck 19 of 23 affirmative defenses in Mr. Hempfling's answer  
12 to the Government's first amended complaint.

13 **Mr. Hempfling's Second Interlocutory Appeal**

14 United States Magistrate Judge Sandra Snyder's ("Judge Snyder's") July 5, 2007 order struck  
15 Mr. Hempfling's jury demand. On August 2, 2007, Mr. Hempfling filed his notice for an interlocutory  
16 appeal of striking his jury demand. The Ninth Circuit's September 19, 2007 order directed Mr.  
17 Hempfling to dismiss his appeal or to show cause why it should not be dismissed for lack of jurisdiction.

18 **Mr. Hempfling's Responses To The Government's Discovery**

19 On October 22, 2007, the Government propounded its first sets of interrogatories and document  
20 requests to Mr. Hempfling. The Government's interrogatories sought names and addresses of purchasers  
21 of Mr. Hempfling's alleged tax fraud schemes. The Government's document requests sought plans and  
22 arrangements of Mr. Hempfling's alleged tax fraud schemes along with documents as to the creation and  
23 finances of Free Enterprise Society, Mr. Hempfling's business name.

24 Defense counsel's November 9, 2007 letter informed the Government's counsel that Mr.  
25 Hempfling would not respond to the Government's discovery due to the pending appeal of striking Mr.  
26 Hempfling's jury demand. Defense counsel wrote:

27 Further, it is our position that the District Court currently has no jurisdiction in  
28 this matter until and unless the 9<sup>th</sup> Circuit Court of Appeals remands the case for further  
proceedings. To this end, **my client intends to maintain a posture of non-**

1       **acquiescence** to the discovery requests until the District Court regains jurisdiction in this  
2 matter, after which you will need to serve these discovery requests again, if you still have  
such desire. (Bold added.)

3       On January 4, 2008, the Government filed its motion to compel Mr. Hempfling's responses to  
4 the Government's interrogatories and document requests. On January 14, 2008, the Ninth Circuit  
5 dismissed Mr. Hempfling's appeal of striking the jury demand.

6       Judge Snyder's January 30, 2008 order granted the Government's motion to compel and ordered  
7 Mr. Hempfling to serve his responses to the Government's interrogatories and document requests no  
8 later than February 4, 2008, the close of non-expert discovery. Judge Snyder noted that Mr. Hempfling  
9 "has neither specifically objected nor responded to any of the discovery requests" and "completely failed  
10 to respond to the discovery requests" to relieve the Government of Local Rule 37-251's joint statement  
11 requirements. Judge Snyder rejected Mr. Hempfling's "argument that the Court was or is without  
12 jurisdiction over the action" and found Mr. Hempfling's "position with respect to the effect of the appeal  
13 on jurisdiction was not substantially justified." Of particular importance, Judge Snyder ruled:

14           [Mr. Hempfling] has failed to respond to the discovery requests, has not objected  
15 to any of them, and has thus waived any objections to the discovery requests. A failure  
16 to object to discovery requests within the time required constitutes a waiver of any  
objection. Richmark Corp. v. Timber Falling Consultants, 959 F.2d 1468, 1473 (9<sup>th</sup> Cir.  
1992).

17       On February 2, 2008, Mr. Hempfling served by electronic mail unsigned copies of his responses  
18 to the Government's interrogatories and document requests.

19       The Government's Interrogatory No. 1 seeks the identity of the person(s) responding to the first  
20 set of interrogatories. Mr. Hempfling responded:

21       Hempfling declines to answer and will invoke his absolute constitutionally protected fifth  
22 amendment right not to testify against himself on the grounds that he does not wish to  
provide any evidence or link in a chain of information that may possibly be used against  
23 him in a criminal prosecution. Additionally see Hempfling's 4<sup>th</sup> affirmative defense in  
the amended answer. Also see Internal Revenue Service *ABUSIVE TAX PROMOTIONS*  
*Student Guide* (Training 3118b-002 Re 8-2000) on file with the court. Moreover, this  
24 response is incorporated in all the following responses whether or not indicated in the  
following responses.  
25

26       The Government's Interrogatory No. 2 seeks the names and addresses of purchasers of the W4  
27 Alternative Withholding Package, an alleged fraudulent tax avoidance scheme, from the Free Enterprise  
28 Society during 2000-2007. Mr. Hempfling responded: "See response to interrogatory number 1.

1 Without waiving said absolute rights, Hempfling has no recollection of said persons or entities."

2 The Government's Interrogatory No. 7 seeks all facts concerning the relationship between Mr.  
3 Hempfling and the Free Enterprise Society. Mr. Hempfling responded: "See response to interrogatory  
4 number 2. Without waiving said absolute rights, see Free Enterprise Society Catalog pursuant to  
5 government's request for production of documents and provided herewith as Exhibit 'A.'"

6 The Government's Document Request Nos. 1-3 seek all versions of three alleged fraudulent tax  
7 scheme packages sold by the Free Enterprise Society – the W4 Alternative Withholding, the IRS Lien  
8 and Levy and the Reliance 2000 packages. Mr. Hempfling responded to the document requests:

9 Said documents to the extent they exist (which the defendant neither admits or denies)  
10 will be made available to the government at a neutral public place at which time the  
11 government will be allowed to copy said documents. Additionally, the act of forcing  
12 Hempfling to admit that said documents exist or are in his possession or that they are  
13 authentic is sufficiently testimonial to warrant absolute 5<sup>th</sup> Amendment protection. Also  
14 see Defendant's 4<sup>th</sup> affirmative defense in the amended answer. Defendant proposes that  
15 the parties meet at offices of the United States Attorney for the Eastern District of  
California, 2500 Tulare Street, Suite 4465, Fresno, California 93721 at 11:00 a.m., for  
purposes of complying with the government's request for documents. Moreover, the  
government is advised that production of documents to the extent they exist, which  
defendant neither admits or denies, will be produced consistent with the invocation of  
defendant's constitutionally protected rights. Again see Defendant's 4<sup>th</sup> affirmative  
defense in the amended answer.

16 Mr. Hempfling has produced to the Government only the Free Enterprise Society's Catalog #10.

17 **Mr. Hempfling's Failure To Appear At His Deposition**

18 On January 10, 2008, the Government served by electronic, overnight and U.S. mail a notice for  
19 Mr. Hempfling's deposition for January 31, 2008 at 9 a.m. at the U.S. Attorney offices in Fresno. By  
20 a January 29, 2008 amended notice served by electronic and overnight mail, the Government reset the  
21 deposition for 11 a.m. on January 31, 2008. Mr. Hempfling did not appear for his deposition.

22 On January 31, 2008, Mr. Hempfling informed the Government's counsel by telephone that Mr.  
23 Hempfling would answer the Government's interrogatories and document requests and would appear  
24 for a February 4, 2008 deposition.

25 Mr. Hempfling appeared at his February 4, 2008 deposition without counsel to preclude his  
26 deposition. By telephone, Judge Snyder advised the Government's counsel to proceed with a F.R.Civ.P.  
27 37(d) sanctions motion.

28 Mr. Hempfling neither sought a protective order nor served a privilege log as to the

1 Government's discovery. The non-expert discovery deadline passed February 4, 2008.

2 **DISCUSSION**

3 \_\_\_\_\_ As discussed below, Mr. Hempfling has obstructed the Government's legitimate discovery and  
4 pursuit of its claims. Mr. Hempfling faults the Government for an absence of evidence "to support its  
5 wild claims" but ignores that his obstruction contributes to such purported absence. Mr. Hempfling fails  
6 to dispute the substantive merits of the Government's claims and makes frivolous claims that the  
7 Government relies on inadmissible hearsay. Certainly, the Government does not offer the tax shelters  
8 and schemes and statements attributed to Mr. Hempfling and Free Enterprise Society for their truth but  
9 rather to demonstrate that they are party-opponent statements and subject to injunction. The purported  
10 absence of evidence is a matter of Mr. Hempfling's making for which he will be sanctioned to support  
11 the Government's requested injunctive relief. Mr. Hempfling's claims that the Government fails to  
12 follow rules and provide discovery fall on deaf ears given Mr. Hempfling's continuing obstruction and  
13 failure to raise substantive disputes with the Government's requested relief.

14 **Failure To Participate In Discovery**

15 F.R.Civ.P. 37(d)(1)(A) empowers a court to "order sanctions" if a party "fails, after being served  
16 with proper notice, to appear for that person's deposition" or fails to serve answers to interrogatories and  
17 document requests. Such failure "is not excused on the ground that the discovery sought was  
18 objectionable, unless the party failing to act has a pending motion for a protective order under Rule  
19 26(c)." F.R.Civ.P. 37(d)(2). Sanctions may include those provided in F.R.Civ.P. 37(b)(2)(A)(i)-(vi).  
20 F.R.Civ.P. 37(d)(3).

21 A party who fails to appear for a deposition is subject to sanctions even in the absence of a prior  
22 order. F.R.Civ.P. 37(d); *Hilao v. Estate of Marcos*, 103 F.3d 762, 764-765 (9<sup>th</sup> Cir. 1996) (unexplained  
23 failure to appear at deposition in contempt proceeding justified sanction deeming allegations to be  
24 established); *Henry v. Gill Industries, Inc.*, 983 F.2d 943, 947 (9<sup>th</sup> Cir. 1993).

25 **Discovery Sanctions**

26 Under F.R.Civ.P. 37(b)(2), if a party "fails to obey an order to provide or permit discovery" a  
27 court "may issue further and just orders," including to :

28 1. Direct as established matters embraced in the order or other designated facts;

- 1        2. Prohibit the disobedient party to support or oppose designated claims or defenses;
- 2        3. Prohibit the disobedient party from introducing designated matters in evidence;
- 3        4. Strike pleadings in whole or part;
- 4        5. Stay further proceedings until an order is obeyed;
- 5        6. Dismiss an action or proceeding in whole or part;
- 6        7. Render a default judgment against the disobedient party; or
- 7        8. Treat as contempt of court the failure to obey an order (except an order to submit to a  
8              mental or physical examination).

9 F.R.Civ.P. 37 authorizes a district court, in its discretion, to impose a wide range of sanctions when a  
10 party fails to comply with the rules of discovery or with court orders enforcing those rules. *National*  
11 *Hockey League v. Metropolitan Hockey Club, Inc.*, 427 U.S. 639, 96 S.Ct. 2778 (1976); *Wyle v. R.J.*  
12 *Reynolds Industries, Inc.*, 709 F.2d 585, 589 (9<sup>th</sup> Cir. 1983); *United States v. Sumitomo Marine & Fire*  
13 *Insurance Co.*, 617 F.2d 1365, 1369 (9<sup>th</sup> Cir. 1980).

14        Although the central factor to a F.R.Civ.P. 37(b)(2) sanction is “justice,” *Valley Engineers, Inc.*  
15 *v. Electric Engineering Co.*, 158 F.3d 1051, 1056 (9<sup>th</sup> Cir. 1998), *cert. denied*, 526 U.S. 1064, 119 S.Ct.  
16 1455 (1999), the sanction “must be specifically related to the particular ‘claim’ which was at issue in  
17 the order to provide discovery.” *Insurance Corp. v. Compagnie Des Bauxites*, 456 U.S. 694, 707, 102  
18 S.Ct. 2099 (1982). The Ninth Circuit Court of Appeals has explained the need for F.R.Civ.P. 37(b)(2)  
19 sanctions:

20        Litigants who are willful in halting the discovery process act in opposition to the  
21 authority of the court and cause impermissible prejudice to their opponents. It is even  
22 more important to note, in this era of crowded dockets, that they also deprive other  
litigants of an opportunity to use the courts as a serious dispute-settlement mechanism.

23 *G-K Properties v. Redevelopment Agency of the City of San Jose*, 577 F.2d 645, 647 (9<sup>th</sup> Cir. 1978).

24        “Where it is determined that counsel or a party has acted willfully or in bad faith in failing to  
25 comply with rules of discovery or with court orders enforcing the rules or in flagrant disregard of those  
26 rules or orders, it is within the discretion of the trial court to dismiss the action or to render judgment  
27 by default against the party responsible for noncompliance.” *G-K Properties*, 577 F.2d at 647. “Where  
28 the drastic sanctions of dismissal or default are imposed . . . the losing party’s non-compliance must be

1 due to willfulness, fault or bad faith.” *Henry v. Gill Industries, Inc.*, 983 F.2d 943, 946 (9<sup>th</sup> Cir. 1993);  
2 *Fjelstad v. American Honda Motor Co.*, 762 F.2d 1334, 1337 (9<sup>th</sup> Cir. 1985). “[D]isobedient conduct  
3 not shown to be outside the control of the litigant is all that is required to demonstrate willfulness, bad  
4 faith, or fault.” *Henry*, 983 F.2d at 948 (quoting *Fjelstad*, 762 F.2d at 1341.) A single willful violation  
5 may suffice depending on the circumstances. *Valley Engineers*, 158 F.3d at 1056.

6 In *National Hockey League*, 427 U.S. at 643, 96 S.Ct. 2778, the United States Supreme Court  
7 explained the rationale for severe F.R.Civ.P. 37(b)(2) sanctions:

8 . . . as in other areas of the law, the most severe in the spectrum of sanctions provided by  
9 statute or rule must be available to the District Court in appropriate cases, not merely to  
penalize those whose conduct may be deemed to warrant such a sanction, but to deter  
those who might be tempted to such conduct in the absence of such deterrent.  
10

11 Nonetheless, sanctions which interfere with “a litigant’s claim or defenses violate due process when  
12 imposed merely for punishment of an infraction that did not threaten to interfere with the rightful  
13 decision of the case.” *Wyle*, 709 F.2d at 591.

14 Dismissal and default judgment are authorized only in “extreme circumstances.” See *Fjelstad*,  
15 762 F.2d at 1338. “So, too, are orders taking the plaintiff’s allegations as established and awarding  
16 judgment to the plaintiff on that basis.” *United States v. Kahaluu Constr. Co., Inc.*, 857 F.2d 600, 603  
17 (9<sup>th</sup> Cir. 1988). Terminating sanctions are appropriate where a “pattern of deception and discovery abuse  
18 made it impossible” for the district court to conduct a trial “with any reasonable assurance that the truth  
19 would be available.” See *Anheuser-Busch, Inc. v. Natural Beverage Distributors*, 69 F.3d 337, 352 (9<sup>th</sup>  
20 Cir. 1995). A terminating sanction under Rule 37(d) is proper “for a serious or total failure to respond  
21 to discovery even without a prior order.” *Siglano v. Mendoza*, 642 F.2d 309, 310 (9<sup>th</sup> Cir. 1981). To  
22 determine whether to impose a severe sanction of dismissal or default, a court considers:

- 23 1. The public’s interest in expeditious resolution of litigation;  
24 2. The court’s need to manage its docket;  
25 3. The risk of prejudice to the party seeking sanctions;  
26 4. The public policy favoring disposition of cases on their merits; and  
27 5. The availability of less drastic sanctions.

28 *Valley Engineers*, 158 F.3d at 1057; *In re Exxon Valdez*, 102 F.3d 429, 433 (9<sup>th</sup> Cir. 1996); *Henry*, 983

1 F.2d at 948; *Kahaluu Constr.*, 857 F.2d at 603; *Thompson v. Housing Auth. of City of Los Angeles*, 782  
2 F.2d 829, 831 (9<sup>th</sup> Cir.), *cert. denied*, 479 U.S. 829, 107 S.Ct. 112 (1986).

3 “What is most critical for case-dispositive sanctions, regarding risk of prejudice and of less  
4 drastic sanctions, is whether the discovery violations ‘threaten to interfere with the rightful decision of  
5 the case.’” *Valley Engineers*, 158 F.3d at 1057 (quoting *Adriana International Corp. v. Thoeren*, 913  
6 F.2d 1406, 1412 (9<sup>th</sup> Cir. 1990), *cert. denied*, 498 U.S. 1109, 111 S.Ct. 1019 (1991)). Prejudice arises  
7 when the ability to go to trial of the party seeking F.R.Civ.P. 37(b)(2) sanctions is impaired. *Adriana*  
8 *International*, 913 F.2d at 1412. “Failure to produce documents as ordered, however, is considered  
9 sufficient prejudice. . . . [C]ontinuing refusal to comply with court-ordered production of documents  
10 constitutes interference with the rightful decision of the case.” *Adriana International*, 913 F.2d at 1412.  
11 However, delay alone does not warrant a terminating sanction. See *Kahaluu Constr.*, 857 F.2d at 604;  
12 *Mir v. Fosburg*, 706 F.2d 916, 919, n. 2 (9<sup>th</sup> Cir. 1983).

13 A three-part analysis determines whether a court “properly considered the adequacy of less  
14 drastic sanctions: (1) did the court explicitly discuss the feasibility of less drastic sanctions and explain  
15 why alternative sanctions would be inappropriate, (2) did the court implement alternative sanctions  
16 before ordering dismissal, and (3) did the court warn the party of the possibility of dismissal before  
17 actually ordering dismissal?” *Adriana International*, 913 F.2d at 1412-1413. “But despite all this  
18 elaboration of factors, we have said that it is not always necessary for the court to impose less serious  
19 sanctions first, or to give any explicit warning.” *Valley Engineers*, 158 F.3d at 1057.

20 With these standards in mind, this Court turns to the Government’s grounds to seek a terminating  
21 sanction.

22 The Government argues that Mr. Hempfling delayed this action’s progress by eight months with  
23 his “frivolous interlocutory appeal from denial of his second motion to dismiss” and caused further delay  
24 with his second interlocutory appeal of the jury demand strike in a case seeking merely injunctive relief.  
25 The Government notes that Mr. Hempfling unreasonably asserted his second interlocutory appeal  
26 deprived this Court of jurisdiction to avoid responding to the Government’s discovery and continued  
27 to assert such “bogus” argument to oppose the Government’s motion to compel. The Government points  
28 to Mr. Hempfling’s improper Fifth Amendment objection to the Government’s discovery after Judge

1 Snyder ordered Mr. Hempfling to respond and advised that Mr. Hempfling had waived objections. The  
2 Government points to Mr. Hempfling's willful failure to attend his January 31, 2008 deposition and  
3 production of only one document – Free Enterprise Society's Catalog #10. The Government contends  
4 that Mr. Hempfling's conduct has "resulted in a total failure of discovery that has prevented the United  
5 States from developing this case for trial." The Government concludes that a sanction lesser than default  
6 judgment will not "restore the integrity of the discovery process."

7 The Government is correct – Mr. Hempfling's conduct has been blatantly egregious. This Court  
8 does not take seriously Mr. Hempfling's comment that "the Government waited until the last minute to  
9 engage in discovery and when faced with Hempfling's objections . . . panicked and went to this Court  
10 to resolve their self made problem." Mr. Hempfling has engaged in delay tactics and subterfuge to  
11 thwart the Government's legitimate discovery and in turn, pursuit of its claims. Mr. Hempfling filed two  
12 meritless interlocutory appeals as a platform to claim frivolously this Court's lack of jurisdiction and  
13 "to maintain a posture of non-acquiescence to the discovery requests." At a minimum, Mr. Hempfling  
14 has toyed with Judge Snyder's discovery orders to amount to disobedience of them. Despite waiving  
15 objections and Judge Snyder's findings of waiver, Mr. Hempfling continued to assert meritless  
16 objections to attempt invalidly to avoid the Government's discovery. The limited information Mr.  
17 Hempfling provided the Government, after he was ordered to do so, was charitably vague and confusing.  
18 As to specific tax avoidance packages sought by the Government, Mr. Hempfling played games with  
19 his responses "to the extent they exist, which defendant neither admits or denies." The ultimate game  
20 playing was evidenced by his deposition, including failure to appear followed by failure of his counsel  
21 to attend to preclude it prior to the non-expert discovery cutoff.

22 Quite simply, Mr. Hempfling acted willfully and in bad faith to comply with discovery rules and  
23 orders to avoid disposition of this action. None of the delay or resulting prejudice to the Government  
24 was outside Mr. Hempfling's control. Mr. Hempfling has chosen a pattern of gamesmanship and  
25 deception to obstruct rightful decision of this action. Contrary to Mr. Hempfling assertions, the  
26 Government's complaints are not based on "deceit and misrepresentations."

27 The public policy factors enumerated above justify default judgment. Mr. Hempfling's  
28 disobedience and mockery of discovery plague this Court and the Government and resolution of this

1 action on the merits with unjustified delay and Court intervention into basic discovery. Mr. Hempfling's  
2 obstruction has diverted Judge Snyder and this Court's attention from other matters and thwarted  
3 management of this Court's docket and unnecessarily added to the heavy caseload burdens of Judge  
4 Snyder and this Court. The Government's prejudice continues with its inability to conduct meaningful  
5 discovery to pursue its claims. This Court's January 4, 2008 order admonished Mr. Hempfling that this  
6 "Court will not allow Mr. Hempfling to use such tactics to avoid cooperating with the Government's  
7 discovery requests and to delay further this 2½ year old litigation." Such admonishment mitigates the  
8 policy of disposition of cases on their merits, especially after the Ninth Circuit dismissed Mr.  
9 Hempfling's appeals out of hand. In light of Mr. Hempfling's repeated and willful failure to cooperate  
10 in basic discovery, even after ordered to do so, less drastic sanctions would serve no purpose other than  
11 to reward Mr. Hempfling's game playing and to promote delay and the Government's prejudice. Like  
12 the Government, this Court is unconvinced that lesser sanctions will provoke Mr. Hempfling to fulfill  
13 his discovery obligations and in turn a rightful decision on the merits of the Government's claims. No  
14 lesser sanction could return the Government to a position had Mr. Hempfling cooperated in discovery  
15 given Mr. Hempfling's history and pattern of grossly insufficient discovery responses rendering them  
16 non-responsive. Mr. Hempfling has chosen gamesmanship over a legitimate attempt to defend the  
17 Government's claims. Mr. Hempfling must face the consequences of his conduct – default judgment.

## **Tax Scheme Injunction**

Having found the Government is entitled to a terminating sanction, this Court turns its attention to injunctive relief for the Government. The Government seeks to permanently enjoin Mr. Hempfling to sell the W4 Alternative Withholding Package, IRS Lien and Levy Package, Reliance 2000 Program, and 16<sup>th</sup> Amendment Reliance Package and seeks information regarding purchasers of the packages. 26 U.S.C. § 7408(a), (b) and (c)<sup>2</sup> empowers a court to enjoin conduct subject to penalty under sections 6700 and 6701 to prevent recurrence of such conduct. Section 7408(b) also entitles a court to enjoin “any other activity subject to penalty” under U.S. Code Title 26. Section 6700 penalizes a person who organizes “a partnership or other entity,” “investment plan or arrangement,” or “any other plan or

<sup>2</sup> Unless otherwise noted, all further statutory references will be to the Internal Revenue Code, Title 26 of the U.S. Code.

1 arrangement” and makes or furnishes a statement about tax consequences by participating in the plan  
2 or arrangement “which the person knows or has reason to know is false or fraudulent as to any material  
3 matter.” In sum, section 7408(a) authorizes the Government to seek an injunction on the grounds that  
4 the defendant has engaged in conduct subject to penalty under section 6700. If a district court finds that  
5 the defendant has engaged in such conduct and that injunctive relief is appropriate to prevent its  
6 recurrence, the court may enjoin the defendant from engaging in it or in any other activity subject to  
7 penalty under section 6700. 26 U.S.C. § 7408(b); *United States v. White*, 769 F.2d 511, 514-515 (8<sup>th</sup> Cir.  
8 1985). “Congress designed section 6700 as a ‘penalty provision specifically directed toward promoters  
9 of abusive tax shelters *and other abusive tax avoidance schemes.*’” *White*, 769 F.2d at 515 (italics in  
10 original.)

“ ‘When an injunction is explicitly authorized by statute, proper discretion usually requires its issuance if the prerequisites for the remedy have been demonstrated and the injunction would fulfill the legislative purpose.’ ” *United States v. Buttorff*, 761 F.2d 1056, 1059 (5<sup>th</sup> Cir. 1985) (citing *Donovan v. Brown Equipment & Service Tools, Inc.*, 666 F.2d 148, 157 (5th Cir.1982)). To obtain an injunction under sections 6700 and 7408, the Government must prove:



<sup>23</sup> *United States v. Estate Preservation Services*, 202 F.3d 1093, 1098 (9<sup>th</sup> Cir. 2000).

24 This Court will review such factors although Mr. Hempfling fails to address them.

### **Organization Or Sell Of A Plan Or Arrangement**

26 The Government argues that advertisements on Free Enterprise Society's website demonstrate  
27 that Mr. Hempfling sells a plan or arrangement subject to section 6700. The Government contends that  
28 Mr. Hempfling's sales of materials are a section 6700(a)(1)(a) "plan or arrangement" because the

1 materials “falsely tell” customers that they are not required to file income tax returns and pay taxes and  
2 that they can purchase a legal defense to not filing returns or paying tax. The Government points to  
3 *United States v. Raymond*, 228 F.3d 804, 811 (7<sup>th</sup> Cir. 2000), where the Seventh Circuit Court of  
4 Appeals addressed a “De-Taxing America Program” which “assured readers that the federal government  
5 is without authority to tax them and that by following the instructions outlined in the Program  
6 individuals can legally refuse to pay federal income and social security tax.” The Seventh Circuit  
7 concluded that the sale of the program to 55 customers “is the sale of an interest in a plan that constitutes  
8 a tax shelter as defined by § 6700(a)(1)(B).”

## **Tax Benefit Statements**

“Section 6700 penalizes any person who makes statements regarding tax benefits of an arrangement organized or sold by him which he knows or has reason to know are false or fraudulent as to any material matter.” *United States v. Buttorff*, 761 F.2d 1056, 1059 (5<sup>th</sup> Cir. 1985). The Government attributes the following as false or fraudulent statements in Mr. Hempfling’s materials, including the Reliance 2000 and W4 Alternative Withholding packages and seminars:



24 The Government further notes that the Free Enterprise Society website states:

25 One of the IRS secrets is the fact that the W4 form has very limited use. If you are an  
26 American you should be using a statement instead. This can mean more take home pay  
as this procedure stops the federal withholding from your paycheck! Package includes  
all necessary forms and instructions for its use.

28 The Government attributes the four-step Reliance 2000 Program to incite and assist customers

1 “to commit willful failure to file and tax evasion.” The Government points to Free Enterprise Society  
2 legal defense director Mr. Hill’s seminar statement to teach customers about “bullet proofing”  
3 themselves against the IRS. At the seminar, Mr. Hempfling offered the Reliance 2000 Package as a  
4 “failure-to-win kit.” For non-filing clients, Mr. Hempfling noted that “[t]his is the minimum, if you’re  
5 a non-filer, we’d like you to do.”

6 The Government notes that the Reliance 2000 program is marketed to invoke the defense in  
7 *United States v. Cheek*, 498 U.S. 192, 111 S.Ct. 604 (1991), that an honest, good faith belief that tax  
8 payment or tax return filing was required defeated a “willfulness” finding. The Government argues that  
9 the Reliance 2000 Program is a packaged “Cheek defense predicated on teaching customers how to  
10 hoodwink a jury.” The Government points to the Reliance 2000 Package’s first step to buy and read the  
11 two-volume *The Law That Never Was*, which Mr. Hempfling sells at his seminars for \$50-\$80.  
12 According to the Government, the books “falsely conclude that the Sixteenth Amendment was never  
13 ratified” and that Mr. Hempfling stresses that “understanding and being able to argue that the Sixteenth  
14 Amendment was never ratified is the first step in winning a failure to file case in court.”

15 The Government notes the Reliance 2000 Package’s second step to buy the 16<sup>th</sup> Amendment  
16 Reliance Package which sells for \$250 at Mr. Hempfling’s seminars and on the Free Society Enterprise  
17 website. The Government characterizes the Reliance 2000 Package as a design to present at a willful  
18 failure to file trial. The Government attributes Mr. Hempfling to indicate that the Reliance 2000  
19 Package is “for show” in that customers can “pretend” they relied on the package.

20 The Government contends that Reliance 2000 Package’s remaining steps are designed to deceive  
21 jurors that the customer “honestly and actively sought to determine the legality of the Sixteenth  
22 Amendment.” The Government notes that the package’s third step includes the buying for \$50-\$75 the  
23 *Redress of Grievance Letter Package*, which includes letters for the customer to send to the President,  
24 Senators, Congressmen, and taxing agencies to question the Sixteenth Amendment’s legal status. The  
25 package’s final step, available only to Free Enterprise Society members who join its Civil Support  
26 Service, involves filing a federal lawsuit to demand whether the Sixteenth Amendment has been ratified.  
27 The Government notes Mr. Hempfling’s seminar statement:

28 But anyway, on your end, what we have to do is impress the jury. This lawsuit is \$150.

1 That will do the complaint for you, give you instructions on how to file it, and when the  
2 U.S. Attorney puts in his reply brief, if you'll put in a motion to dismiss, we will give  
3 you the reply brief and everything else included in that hundred and fifty. And usually  
4 they will dismiss it at that point. If they don't, so far we've just supplied the additional  
paperwork on anything they've asked us for. Because **we're not actually trying to win**  
that, because, you know, there is no law. (Bold added.)  
4

5 The Government concludes that Mr. Hempfling's admission that a lawsuit will be lost demonstrates the  
6 absence of a good faith defense to tax charges.

7 **Scienter To Violate Section 6700**

8 The Government argues that it need not show that Mr. Hempfling acted with subjective bad faith,  
9 that is, that he actually knew when he organized and sold the packages that they contained false and  
10 fraudulent statements concerning tax benefits availability or internal revenue law requirements. The  
11 Government holds itself to a lower standard whether a reasonable person in Mr. Hempfling's subjective  
12 position would have discovered the falsity of his statements.

13 Factors to determine requisite scienter to violate section 6700 include:

- 14 1. Extent of defendant's reliance on knowledgeable professionals;  
15 2. Defendant's level of sophistication and education; and  
16 3. Defendant's familiarity with tax matters.

17 *Estate Preservation*, 202 F.3d at 1103.

18 The Government notes that Mr. Hempfling does not claim that he relied on professionals  
19 knowledgeable in tax law. The Government points out that Mr. Hempfling is a Free Enterprise Society  
20 founder and has frequently lectured on "requirements of the internal revenue law and their workings."  
21 The Government argues that Mr. Hempfling "had every reason to know that the statements about the  
22 requirements of the internal revenue laws and the Sixteenth Amendment that were contained in the  
23 products which he sold through [Free Enterprise Society] were false." The Government notes that the  
24 Internal Revenue Code and case law "leave no room to doubt that all citizens with more than minimal  
25 income are subject to tax laws." The Government cites the following:

26 We find it hard to understand why the long and unbroken line of cases upholding  
27 the constitutionality of the sixteenth amendment generally, *Brushaber v. Union Pacific*  
28 *Railroad Company*, 240 U.S. 1, 36 S.Ct. 236, 60 L.Ed.2d 493 (1916), and those  
specifically rejecting the argument advanced in [Mr. Benson's] *The Law That Never  
Was*, have not persuaded Miller and his compatriots to seek a more effective forum for

1 airing their attack on the federal income tax structure.

2 *Miller v. United States*, 868 F.2d 236, 241 (7<sup>th</sup> Cir. 1989); *see United States v. Dunkel*, 927 F.2d 955,  
3 955 (7<sup>th</sup> Cir. 1991) (“district judges may rebuff defenses based on erroneous constitutional beliefs (such  
4 as that the 16<sup>th</sup> Amendment was not properly ratified)”); *United States v. Schiff*, 876 F.2d 272, 275 (2<sup>nd</sup>  
5 Cir. 1989) (“The payment of income taxes is not optional . . . and the average citizen knows that the  
6 payment of income taxes is legally required.”).

7 **Materiality**

8 To support materiality of Mr. Hempfling’s statements, the Government points to:

- 9 1. The W4 Alternative Withholding Package statement that United States citizens  
10 domiciled in the United States are exempt from withholding of income and Social  
11 Security taxes from their wages;
- 12 2. The IRS Lien and Levy Package statement that IRS liens and levies are legally  
13 unenforceable; and
- 14 3. The Reliance 2000 Program statement that the Sixteenth Amendment was not ratified.

15 Section 6700 is violated by engaging in the sale of any investment plan by furnishing statements  
16 about tax benefits which the person knows or has reason to know are false or fraudulent as to any  
17 material matter. *United States v. Smith*, 657 F.Supp. 646, 655 (W.D. La. 1986). To prove materiality,  
18 the Government “need not demonstrate that a purchasing taxpayer has relied on the purported  
19 misrepresentations.” *Smith*, 657 F.Supp. at 655. Rather, “a matter is considered material to the  
20 arrangement ‘if it would have a substantial impact on the decision making process of a reasonably  
21 prudent investor.’” *United States v. Buttorff*, 761 F.2d 1056, 1062 (citing S.Rep. No. 97-494, 97th  
22 Cong.2d Sess. 267 (1982), reprinted in 1982 U.S.Code Cong. & Ad.News 781, 1015).

23 **Recurrence**

24 If a defendant engages in conduct subject to a section 6700 penalty, injunctive relief is available  
25 under section 7408(a) if “appropriate to prevent the recurrence of such conduct.” Injunctive relief “is  
26 appropriate and necessary to prevent further financial exploitation at the public’s expense.” *United*  
27 *States v. Buttoff*, 563 F.Supp. 450, 455 (D.C. Tex. 1983). Factors to determine the likelihood of future  
28 section 6700 violations and thus an injunction’s need include:

- 1       1. Gravity of harm caused by the offense;
- 2       2. Extent of defendant's participation;
- 3       3. Defendant's degree of scienter;
- 4       4. Isolated or recurrent nature of infraction;
- 5       5. Defendant's recognition or non-recognition of his/her culpability; and
- 6       6. Likelihood that defendant's occupation would place him/her in a position where future  
7            violations could be anticipated.

8 *Estate Preservation*, 202 F.3d at 1105.

9 To address these factors, the Government notes that Mr. Hempfling:

- 10      1. Is the central figure behind the Free Enterprise Society's creation, promotion and tax-fraud schemes;
- 11      2. Operates Free Enterprise Society as a nationwide multi-level marketing scheme to sell abusive tax schemes which have been routinely rejected by courts;
- 12      3. Continues to sell materials that falsely state the internal revenue law and Sixteenth Amendment are invalid and do not apply;
- 13      4. Maintains that neither he nor his followers are required to file tax returns or pay taxes;
- 14      5. Caused large-scale harm to impede tax collection;
- 15      6. Has acknowledged neither his wrongful conduct nor an intent to cease selling his packages; and
- 16      7. Continues to display "a long-standing antipathy to the federal tax laws and the Sixteenth Amendment that places him in a position where future violations of IRC § 6700 are inevitable."

23      Mr. Hempfling neither addresses the factors for an injunction under sections 6700 and 7408 nor  
24      opposes the Government's grounds for such injunction. As such and in light of the terminating sanction,  
25      the Government's points are considered uncontested to satisfy the elements for sections 6700 and 7408  
26      injunctive relief. The Government's positions on the injunctive relief are entitled to deference to fulfill  
27      statutory purposes to eliminate abusive tax avoidance schemes.

28      ///

## **Section 7402(a) Injunction**

The Government argues that section 7402 injunction relief will properly prevent Mr. Hempfling's interference with tax enforcement and "bilk[ing] money from Hempfling's customers and pav[ing] the way for them to become illegal non-filers." Section 7402(a) authorizes an injunction as "necessary or appropriate for the enforcement of the internal revenue laws." Section 7402 demonstrates "congressional intention to provide the district courts with a full arsenal of powers to compel compliance with the internal revenue laws." *Brody v. United States*, 243 F.2d 378, 384 (1<sup>st</sup> Cir. 1957). Courts have recognized section 7402's broad powers:

9 . . . there need not be a showing that a party has violated a particular Internal Revenue  
10 Code section in order for an injunction to issue. The language of § 7402(a) encompasses  
11 a broad range of powers necessary to compel compliance with the tax laws. See *United*  
12 *States v. First National Bank*, 568 F.2d 853, 855-56 (2d Cir.1977); *Brody v. United*  
13 *States*, 243 F.2d 378, 384 (1st Cir.1957). It has been used to enjoin interference with tax  
14 enforcement even when such interference does not violate any particular tax statute. See  
15 *United States v. Ekblad*, 732 F.2d 562 (7th Cir.1984) (§ 7402 used to enjoin individual's  
harassment of IRS agents designed to hinder their effectiveness); *United States v. Hart*,  
701 F.2d 749 (8th Cir.1983) (same); *United States v. VanDyke*, 568 F.Supp. 820  
(D.Or.1983) (same). Furthermore, the statute has been relied upon to enjoin activities  
of third parties that encourage taxpayers to make fraudulent claims. *United States v.*  
*Landsberger*, 692 F.2d 501 (8th Cir.1982); *United States v. May*, 555 F.Supp. 1008  
(E.D.Mich.1983).

<sup>16</sup> *United States v. Ernst & Whinney*, 735 F.2d 1296, 1300 (11<sup>th</sup> Cir. 1984), *cert. denied*, 470 U.S. 1050, 105 S.Ct. 1748 (1985).

Similar to injunctive relief under sections 6700 and 7408, Mr. Hempfling fails to challenge the merits of section 7402(a) injunctive relief of which the Government is deserving to enforce internal revenue laws. Section 7402(a) further supports the Government's requested injunctive relief.

## **PERMANENT INJUNCTION ORDER**

22 For the reasons discussed above, this Court permanently ENJOINS defendant Steven Hempfling,  
23 d/b/a Free Enterprise Society, and all those in active concert or participation with Steven Hempling to:

- 24       1. Promote, organize or sell the “W4 Alternative Withholding Package,” “IRS Lien and  
25           Levy Package,” “Reliance 2000 Program,” and/or “16<sup>th</sup> Amendment Reliance Package,”  
26           which are abusive tax shelters, or arrangements that advise or encourage attempt to evade  
27           assessment or collection of federal tax:  
28       2. Promote, organize or sell (or to assist therein) any other abusive tax shelter, plan or

1 arrangement that incites an attempt to violate the internal revenue laws, to evade  
2 unlawfully the assessment or collection of federal tax liabilities, or to claim unlawfully  
3 improper tax refunds;

- 4 3. Make false statements about excludability of income, or securing any tax benefit by  
5 reason of participating in such tax shelters, plans or arrangements;  
6 4. Engage in any other activity subject to penalty under Internal Revenue Code § 6700; and  
7 5. Engage in other, similar conduct that substantially interferes with proper administration  
8 of internal revenue laws.

9 **FURTHER ORDERS**

10 In addition, this Court ORDERS defendant Steven Hempfling, no later than March 31, 2008, to:

- 11 6. Deliver (by United States mail, and, if an e-mail address is known, by electronic mail)  
12 at his expense a copy of this permanent injunction order to everyone who purchased the  
13 “W4 Alternative Withholding Package,” “IRS Lien and Levy Package,” “Reliance 2000  
14 Program,” and/or “16<sup>th</sup> Amendment Reliance Package”;  
15 7. Serve the Government a complete list of everyone who purchased from defendant Steven  
16 Hempfling a “W4 Alternative Withholding Package,” “IRS Lien and Levy Package,”  
17 “Reliance 2000 Program,” and/or “16<sup>th</sup> Amendment Reliance Package” and to provide  
18 the Government the purchasers’ names, mailing addresses, e-mail addresses and Social  
19 Security numbers;  
20 8. Remove from the website [www.FreeEnterpriseSociety.com](http://www.FreeEnterpriseSociety.com) all references to “W4  
21 Alternative Withholding Package,” “IRS Lien and Levy Package,” “Reliance 2000  
22 Program,” and/or “16<sup>th</sup> Amendment Reliance Package”; and  
23 9. Post, in not less than 12-point type at the top of the first page of  
24 [www.FreeEnterpriseSociety.com](http://www.FreeEnterpriseSociety.com) a copy of this permanent injunction order.

25 This Court further ORDERS defendant Steven Hempfling, no later than April 14, 2008, to file  
26 and serve his affidavit to detail his compliance with the requirements of subparagraphs 6-9 above.

27     ///

28     ///

1 This Court DIRECTS the clerk to enter judgment in favor of plaintiff United States of America  
2 and against defendant Steven Hempfling.

IT IS SO ORDERED.

4 || Dated: March 12, 2008

/s/ Lawrence J. O'Neill

**UNITED STATES DISTRICT JUDGE**